

DEPARTMENT OF TRANSPORTATION**AUDITS AND INVESTIGATIONS**

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January 10, 2008

Matt Todd, P.E.

Manager of Programming

Alameda County Congestion Management Agency

1333 Broadway, Suite 220

Oakland, California 94612

Re: Preaward Audit – Rajappan & Meyer Consulting Engineers, Inc.

File No.: P1300-0930

Agreement No.: CMA#A07-011.RM.Ph2

Dear Mr. Todd:

We have audited Rajappan & Meyer Consulting Engineers, Inc.'s (Consultant) proposed costs under draft Agreement No. CMA#A07-011.RM.Ph2 with the Alameda County Congestion Management Agency (ACCMA) to determine whether the proposed costs are reasonable in relation to actual historical costs and estimating procedures, and whether the Consultant's financial management system is adequate to accumulate and segregate reasonable, allocable and allowable project costs. We also reviewed the agreement to assess whether the required fiscal provisions are included.

The Consultant management is responsible for the fair presentation of the proposed costs, ensuring compliance with contract provisions and state and federal regulations, and that the financial management system maintained by the Consultant is adequate to accumulate and segregate reasonable, allocable and allowable costs.

Our audit was conducted in accordance with the Performance Standards set forth in the *Government Auditing Standards* issued by the Comptroller General of the United States of America. The audit was less in scope than an audit performed for the purpose of expressing an opinion on the financial statements of the Consultant. Therefore, we did not audit and we are not expressing an opinion on the Consultant's financial statements.

The standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and the records audited are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records selected. It also includes assessing the accounting principles used and significant estimates made by the consultant management, as well as evaluating the overall presentation.

The Consultant shall provide professional services for the Preliminary Engineering, Project Approval, Environmental Clearance and Final Design Services for I-880 South Bound High-Occupancy Vehicle Lane Widening. The total amount of this contract shall not exceed \$2,997,916. Reimbursement is to be made at specified hourly rates of compensation to the following consultants:

Rajappan & Meyer Consulting Engineers, Inc. (Prime)
TJKM Transportation Consultants*
Parikh Consultants, Inc.*
LSA Associates, Inc.*
HMH Civil Engineers*
GeoCon, Inc.*
AEC, Inc.*
Schaaf & Wheeler Consulting Civil Engineers*
Sugimura & Associates Architects*
ARWS, Inc.*

* - Audit waived.

The scope of the audit was limited to financial and compliance activities related to the above referenced agreement. The audit consisted of verifying the proposed costs, an assessment of the accounting principles used, and significant estimates made by the Consultant; as well as, an evaluation of compliance with Code of Federal Regulations (CFR) 49, Part 18 and CFR 48, Chapter 1, Part 31. This audit included a full scope audit of the Consultant. We reviewed the draft agreement, interviewed applicable personnel, and performed limited tests on the Consultant's financial management system and proposed costs as of October 23, 2007. Financial management system and cost proposal changes subsequent to this date were not tested and, accordingly, our conclusion does not pertain to changes arising after this date. We did not audit or examine the proposed indirect rates since a preaward audit is significantly less in scope than an incurred cost audit or examination. We reviewed the proposed indirect rates for the purpose of accepting contract progress billings.

Due to inherent limitation in any financial management system, misstatements due to error or fraud may occur and not be detected. Also, projections of any audit of the financial management system to future periods are subject to the risk that the financial management system may become inadequate due to changes in conditions, or the degree of compliance with policies and procedures may deteriorate.

The results of the audit were communicated with Keith Meyer, Vice President, Rajappan & Meyer Consulting Engineers, Inc., and Liz Brazil, Contracts Administrator, ACCMA, on November 13, 2007. Our findings and recommendations, the Consultant's response, and our analysis of the Consultant's response are set forth in the Attachment to this report.

CONCLUSION

Based on our audit work, we found the required fiscal provisions are included in the draft agreement, except as noted in the Attachment to this report. In addition, the Consultant's proposed costs are reasonable in relation to actual historical costs and estimating procedures

and the Consultant's financial management system is adequate to accumulate and segregate reasonable, allocable, and allowable project costs, except as noted in the Attachment to this report.

This report is intended solely for the information of the ACCMA, the Department of Transportation, and the Federal Highway Administration. However, this report is a matter of public record and its distribution is not limited.

Please forward a copy of the executed agreement and cost proposal to Audits and Investigations. If you have any questions, please contact Linda Laubinger, Audit Manager, at (916) 323-7957.

ORIGINAL SIGNED BY:

Valerie Wong
Auditor

Approved:

ORIGINAL SIGNED BY:

MARYANN CAMPBELL-SMITH
Chief
External Audits

Attachments

c: Sylvia Fung -- DLAE 04
P1300-0930

ATTACHMENT
Preaward Audit Findings and Recommendations
Agreement No.: CMA#A07-011.RM.Ph2

Contract Findings

Finding 1

The agreement start date is not clearly stated in the agreement.

Recommendation: We recommend the start date be identified in the agreement.

Finding 2

There is no clause to identify how other direct costs will be reimbursed in the contract provisions.

Recommendation: We recommend the appropriate language for a method of payment clause, as identified in the Local Assistance Procedures Manual - Chapter 10, Exhibit 10R – A&E Sample Contract Language, Allowable Costs and Payments – Option 3 (on-call contracts), Paragraph D, be incorporated in the agreement.

ATTACHMENT
Precaward Audit Findings and Recommendations
Agreement No.: CMA#A07-011.RM.Ph2

Rajappan & Meyer Consulting Engineers, Inc.

Finding 1

The proposed two percent mark-up on subconsultant costs is unsupported.

Recommendation: We recommend the proposed two percent mark-up on subconsultant costs be removed from the cost proposal.

Auditee's Response: The consultant disagrees with the finding. The consultant's response states that the "2% markup on subconsultants was offered as a standard agreement item by CMA." See attached copy of consultant's complete response.

Auditor's Analysis: The consultant's response does not include additional information to support the proposed markup on subconsultant costs. ACCMA may choose to reimburse the consultant for the markup on subconsultant costs; however, Department funds should not be used for such costs. Consequently, A&I stands by its audit finding.

Finding 2

The proposed indirect rate of 119 percent is misstated. The evaluated indirect rate is 78.29 percent for fiscal year 2006.

Recommendation: We recommend the cost proposal be revised to reflect the evaluated indirect rate noted above.

Auditee's Response: The consultant disagrees with the finding. The consultant's response states their disagreement with the methodology used in our analysis of "executive salaries", "salaries of related administrative employees", and "credit for CADD and printing charges." The consultant's response included a revised overhead calculation, based on the proposed adjustments noted in their response, which reflects an overhead rate of 128%. However, they agreed to accept their originally proposed overhead rate of 119%. See attached copy of the consultant's complete response.

Auditor's Analysis: The consultant's response regarding "executive salaries" provided additional information which was taken into consideration. We revised our analysis to include the consultant's information regarding executive salaries, but there was no impact on the resulting rate. The consultant's response regarding "salaries of related administrative employees" does not include additional information to support the reasonableness of the proposed cost. The consultant's response regarding the "credit for CADD and printing charges" is based on their revised overhead schedule, where they removed the associated costs in lieu of crediting the revenue received. However, our analysis is based on the overhead rate prepared by the consultant's CPA,

ATTACHMENT
Preaward Audit Findings and Recommendations
Agreement No.: CMA#A07-011.RM.Ph2

where the associated costs are not removed. Consequently, A&I stands by its audit findings.

Finding 3

The consultant proposed other direct cost rates for Fax (\$1.00/sheet), Copies (\$.12/sheet), B/W Plots (\$5.00/sheet), and Color Plots (\$15.00/sheet), which are not supported.

Recommendation: We recommend the cost proposal be revised to reflect reimbursement of the other direct costs, as stated in the contract language (see Contract Finding #2 above).

Auditee's Response: Consultant did not respond to finding.



November 19, 2007

MaryAnn Campbell-Smith, Chief
External Audits
California Department of Transportation
1304 O Street, Suite 200
Sacramento, CA 94274

RE: RESPONSE TO DRAFT AUDIT FINDINGS
2006 OH RATE FOR RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.

Dear Ms. Campbell-Smith:

We have reviewed the State's assessment of our 2006 Overhead rate prepared by Valerie Wong and disagree with the findings. Further, we disagree with her interpretation of FAR regulations and guidelines and we stand by our rate as presented herein.

It appears to us that we are being penalized and discriminated against because we are a small and lean minority owned business firm. We firmly believe that our rate and total price is extremely cost-effective for CMA and Caltrans. We are also confident that any other bidder will charge a total project cost well in excess of our proposal, since other firms' OH rates in our business are well in excess of 150%. If that is the direction you choose to go, we do not believe that will be well-received in the public record. We strongly urge you to reconsider and to also look at the overall project cost.

GENERAL COMMENT ABOUT R&M

It should be noted that Rajappan & Meyer Consulting Engineers, Inc. is a unique, closely-held minority owned company. We routinely compete and win against the largest national firms because of our extraordinary capabilities and focus in large project management, not just civil or structural engineering. We have been determined by our clients to be among the top project management firms in Northern California, including among all national firms. This is why you are auditing us, and not URS, Parsons, PBQD or other national firms. That being said, many of your interpretations of certain sections of 48 CFR 31 and the use of PSMJ Benchmarks are unreasonable and unacceptable. I have reviewed the PSMJ salary schedule for all disciplines and it grossly underestimates salary costs in the SF Bay Area.

EXECUTIVE SALARIES

You backed into an effective billing rate of \$78.90 via your compliance testing to calculate indirect labor on principals based on billing rates from contracts that are 1-5 years old. Most contracts for R&M are NOT based on overhead or profit %, rather market rates. Therefore, sometimes 0% profit or negative profitability is achieved for our executives. Your compliance testing assumptions are incorrect, and your results are unrealistic, producing a lower hourly rate than some of our employees. You have also assessed Rajappan & Meyer Consulting Engineers, Inc. executives in comparison to other similarly sized average consulting firms. This is an inappropriate interpretation for the following reasons:

CIVIL, TRAFFIC, STRUCTURAL AND TRANSIT ENGINEERING

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.
1038 LEIGH AVENUE, SUITE 100, SAN JOSE, CA 95126
PH:(408) 280-2772 FX:(408) 904-7215 KRITH@RMENGINEERS.COM



1. We are a high profile project management firm with contracts currently up to \$25 million in fee value, managing dozens of other consultants. We specialize in large projects, normally associated with national firms. You can view the types of projects we do at our website: www.rmengineers.com.
2. Both principals are equal in managing the company and work. There is a named President and Vice President since there can't be two Presidents. Your comparison of us to standard executive class of other large, inefficient firms is not appropriate.
3. We must therefore maintain that the 2006 FAR allowable compensation of \$536,689 per principal is justified and appropriate. The total allowable executive compensation is \$1,093,378. This is particularly appropriate in the SF Bay Area, one of the highest salaried areas in the country.

We offer the following revision:

2006 Direct Labor Billed	Meyer	Rajappan	Total
A. (from payroll register)	\$ 288,184	\$ 377,008	\$ 665,192
B. FAR Compensation Allowance	\$ 536,689	\$ 536,689	\$ 1,093,378
C. B-A = Allowable Indirect	\$ 248,505	\$ 159,681	\$ 408,186

SALARIES OF RELATED ADMINISTRATIVE EMPLOYEES:

Again you have used PMSJ as the benchmark for L. Meyer and S. Nair, with a basis of interpretation being 48 CFR 31.205-6(i)(A). We insist that the salaries paid to all employees be accounted for in full, since those are the actual legitimate overhead costs that we pay. We will however eliminate their bonus pay of \$40,000 in the overhead calculation.

CREDIT FOR CADD AND PRINTING CHARGES:

We believe you have misinterpreted the intent of CFR 31.201-5 (Credits) as the basis for disallowing \$486,553 of income against cost. Since you are not allowing the cost to be charged on overhead, the past revenue received for these services based on our fixed asset cannot be added as a credit to cost. We disagree with you that this amount should be disallowed. CFR 31.201-5 states "The applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund." Again, the vast majority of our contracts are not cost allowance based, therefore application of this rule is inappropriate. Since you are not allowing the cost item to be in our future overhead, the issue is perfectly clear that the income received from these items is not applicable against our overhead.

2% MARKUP ON SUBCONSULTANTS

The 2% markup on subconsultants was offered as a standard agreement item by CMA. If this is to be disallowed, then our profit should be increased to 12%.

CIVIL, TRAFFIC, STRUCTURAL AND TRANSIT ENGINEERING

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.
1038 LEIGH AVENUE, SUITE 100, SAN JOSE, CA 95126
PH: (408) 280-2772 FX: (408) 904-7215 KEITH@RMENGINEERS.COM



REVISED OVERHEAD CALCULATIONS

I have attached a spreadsheet showing our original, your estimate and our revision to the OH rate schedule. We will accept the 125% overhead as noted in our attached spreadsheet. This is a reduction from 128% as shown by our accountant, with their report attached.

REVISED HOURLY RATES

I have attached a spreadsheet showing the revised hourly rates we now calculate for the purpose of invoicing 2007 labor and the labor rates that we will use for project budgeting purposes, for which the hourly rates are increased to the mid-point of the project design using 7% annual increases. Annual adjustments of hourly rates and overhead will be made, starting in January 2008, with the billing rate adjusted accordingly.

Again, we disagree with your proposed findings, calculation methodology and FAR interpretations. We strongly urge you to reconsider and accept our proposed rate, and to also look at the overall project cost in comparison to what other firms will charge. You will find that we will be the lowest proposed cost of any firm for this work with our current proposal to CMA.

Sincerely,

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.

ORIGINAL SIGNED BY:

Keith G. Meyer, P.E.
Vice President

cc: Gloria Miller
Bala Rajappan
Mayer Hoffman & McCann

Rajappan & Meyer Consulting Engineers, Inc.

Comparison of Overhead Rates

31-Oct-07

	Oct 11 2007 Analysis from MHM			Caltrans Analysis		R&M Final Revisions		Notes
	Trial Balance	Adjust	Total	Adjust	Total	Caltrans	Total	
A - DIRECT LABOR	\$ 3,303,995	\$ 743,722	\$ 2,560,273	\$ (189,880)	\$ 2,370,393		\$ 2,370,393	
B - INDIRECT COSTS:								
Fringe Benefits on Direct Labor-								
Health Insurance	\$ 184,951		\$ 184,951		\$ 184,951		\$ 184,951	
401(k) Pension Plan	\$ 282,821	\$ (72,400)	\$ 180,521		\$ 190,521		\$ 190,521	
Bonus	\$ 124,890		\$ 124,890	included in MHM	\$ 124,891	\$ (40,000)	\$ 84,891	Related bonuses of \$40,000 deducted.
Vacation/Sick/Holiday	\$ 476,021	\$ (163,603)	\$ 312,418	\$ 163,603	\$ 476,021		\$ 476,021	
Payroll Taxes	\$ 233,379		\$ 233,379		\$ 233,379		\$ 233,379	
	\$ 1,282,162	\$ (236,003)	\$ 1,046,159	\$ 163,603	\$ 1,209,763		\$ 1,169,763	
C - OPERATING OVERHEAD								
Auto	\$ 47,311		\$ 47,311		\$ 47,311		\$ 47,311	
Bank Charges	\$ 127		\$ 127		\$ 127		\$ 127	
Continuing Education	\$ 875		\$ 875		\$ 875		\$ 875	
Depreciation /Amortization	\$ 131		\$ 131		\$ 131	\$ (131)	\$ -	computer equipment eliminated from OH
Dues & Subscriptions	\$ 2,176		\$ 2,176		\$ 2,176		\$ 2,176	
Equipment	\$ 20,500		\$ 20,500		\$ 20,500	\$ (20,500)	\$ -	computer equipment eliminated from OH
Executive Salaries	\$ 1,093,378	\$ (371,861)	\$ 721,517	\$ (573,190)	\$ 148,327	\$ 259,859	\$ 408,186	FAR allowable salaries added back in, totalled for actual direct and indirect labor
Insurance	\$ 80,749		\$ 80,749		\$ 80,749		\$ 80,749	
Legal & Professional	\$ 160,011		\$ 160,011		\$ 160,011		\$ 160,011	
Office	\$ 15,359		\$ 15,359	\$ (8,483)	\$ 6,876		\$ 6,876	
Postage	\$ 10,051		\$ 10,051	\$ (4,993)	\$ 5,058		\$ 5,058	
Rent	\$ -	\$ 238,869	\$ 238,869	\$ 17,248	\$ 256,117		\$ 256,117	
Salaries		\$ 663,009	\$ 663,009	\$ (404,390)	\$ 258,618	\$ 404,390	\$ 663,009	Direct salaries of all employees added back in.
Software	\$ 27,458		\$ 27,458		\$ 27,458	\$ (27,458)	\$ -	CADD to be eliminated
State Franchise Tax	\$ 7,500		\$ 7,500		\$ 7,500		\$ 7,500	
Storage /Rent	\$ 17,248		\$ 17,248	\$ (17,248)	\$ -		\$ -	
Supplies/Printing	\$ 126,224		\$ 126,224	\$ (55,812)	\$ 70,612	\$ -	\$ 70,612	Printing portion eliminated
Travel	\$ 10,251		\$ 10,251		\$ 10,251		\$ 10,251	
Utilities	\$ 71,005		\$ 71,005		\$ 71,005		\$ 71,005	
Adjustment	\$ -		\$ -	\$ (527,749)	\$ (527,749)	\$ 527,749	\$ -	Income cannot be applied to expenses for expenses not included.
	\$ 1,690,354	\$ 530,017	\$ 2,220,371	\$ (1,574,417)	\$ 645,954	\$ 1,144,040	\$ 1,789,863	
D - TOTAL B+C	\$ 2,972,516	\$ 294,014	\$ 3,266,530	\$ (1,410,814)	\$ 1,855,717	\$ 1,144,040	\$ 2,959,626	
E - OH RATE) D/A			128%		78%		125%	

**RAJAPPAN & MEYER
CONSULTING ENGINEERS, INC.**

**SCHEDULE OF COMPUTATION OF
OVERHEAD MULTIPLIER RATE**

December 31, 2006

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INDEPENDENT ACCOUNTANTS' REPORT

To the Management

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.

We have prepared the schedule of computation of overhead multiplier rate and the accompanying supplemental information for Rajappan & Meyer Consulting Engineers, Inc., solely to assist the Company in complying with Federal Acquisition Regulations, for the year ended December 31, 2006. This engagement was conducted in accordance with the Statements on Standards for Consulting Services established by the American Institute of Certified Public Accountants.

We were not engaged to and did not conduct an audit, the objective of which would be the expression of an opinion on the accompanying schedule of computation of overhead multiplier rate.

This report is intended solely for the information and use of the contracting entities and by management of Rajappan & Meyer Consulting Engineers, Inc. and is not intended to be used by anyone other than these specified parties.

San Jose, California
October 22, 2007

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.

SCHEDULE OF COMPUTATION OF OVERHEAD MULTIPLIER RATE

Year Ended December 31, 2006

	<u>2006</u>	<u>Adjustments</u>	<u>Adjusted Balance</u>	<u>Multiplier</u>
Direct salaries	\$ 2,560,273	\$ -	\$ 2,560,273	1
Payroll Expenses				
Health insurance	\$ 184,951	\$ -	\$ 184,951	
401(k) pension plan	262,921	(72,400)	190,521	
Pension bonus plan	124,890	-	124,890	
Vacation	476,021	(163,603)	312,418	
Payroll taxes	233,379	-	233,379	
	<u>1,282,162</u>	<u>(236,003)</u>	<u>1,046,159</u>	<u>0.41</u>
Other indirect Operating Overhead				
Auto	47,311	-	47,311	
Bank charges	127	-	127	
Continuing education	875	-	875	
Depreciation and amortization	131	-	131	
Dues and subscriptions	2,176	-	2,176	
Equipment	20,500	-	20,500	
Executive salaries	1,093,378	(371,861)	721,517	
Insurance	80,749	-	80,749	
Legal and professional	160,011	-	160,011	
Office	15,359	-	15,359	
Postage	10,051	-	10,051	
Rent	-	238,869	238,869	
Salaries	-	663,009	663,009	
Software	27,458	-	27,458	
State franchise tax	7,500	-	7,500	
Storage rent	17,248	-	17,248	
Supplies and printing	126,224	-	126,224	
Travel	10,251	-	10,251	
Utilities	71,005	-	71,005	
	<u>1,690,354</u>	<u>530,017</u>	<u>2,220,371</u>	<u>0.87</u>
	<u>\$ 2,972,516</u>	<u>\$ 294,014</u>	<u>\$ 3,266,530</u>	<u>1.28</u>

SUPPLEMENTAL INFORMATION

RAJAPPAN & MEYER CONSULTING ENGINEERS, INC.

**ANALYSIS OF COSTS INCLUDED IN COMPUTATION
OF OVERHEAD MULTIPLIER RATE**

Year Ended December 31, 2006

DIRECT SALARIES

Direct labor reflects all wages specifically related to projects.

PAYROLL EXPENSES

Payroll expenses of Rajappan & Meyer Consulting Engineers, Inc. (the Company) are comprised of employee health insurance costs, pension plan contributions, vacation, and payroll taxes. Information regarding these expenses was gathered directly from the Company's expense reports. Adjustments were made to exclude the benefits for pension plan contributions of \$72,400 and vacation of \$163,603 received by executives, as those benefits are included as part of their compensation.

OTHER INDIRECT OPERATING OVERHEAD

Other indirect operating overhead was compiled directly from the Company's expense reports. The expenses included in the computation of overhead multiplier rate are only those allowable per Federal Acquisition Regulations. Un-allowable costs were not included.

The building is owned by the same two principals who own the Company, and therefore the common ownership requires us to consider the building as owned by the Company. Since the Company occupies the entire building, all allowable expenses related to ownership of the building have been included.

Material expenses that do not specifically correspond to the Company's expense reports are executive salaries, rent, and salaries.

Depreciation for the purposes of the overhead calculation is the amount from the Company's federal tax return.

The Company is organized as an S-Corporation and therefore its principals, or senior executives, are compensated with a combination of salary and distributions of the Company's equity. Per Federal Acquisition Regulations, the maximum allowable compensation for a senior executive is \$546,689. Therefore, the maximum allowable indirect compensation for the Company's two executives is \$721,517 (\$1,093,378 less executive direct salaries of \$371,861). Salaries of \$663,009 include all non-executive salaries allocated to overhead, as indicated on payroll reports.

Rent expense of \$238,869 for the purpose of the overhead calculation include \$142,389 (facilities cost of money), \$67,944 and \$28,536 (depreciation & property taxes, respectively, included on the tax return for the partnership which owns the building). As indicated in Federal Acquisitions Regulations (FAR), "facilities cost of money is an imputed cost determined by applying the cost of money rate to facilities employed in contract performance." FAR allows the inclusion of this calculation, regardless if it is not kept on the Company's books. The facilities cost of money of \$142,389 has been calculated with interest rates published by the United States Treasury.